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No. 92-551

In the

Supreme Court of the United States

October Term, 1992

JACK F. KEMP, SECRETARY OF THE UNITED STATES DEPARTMENT OF HOUSING AND URBAN DEVELOPMENT, ET AL.,

Petitioners,

v.

ALPINE RIDGE GROUP, ET AL.,

Respondents.

OPPOSITION TO THE PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE NINTH CIRCUIT

Respondent Acacia Villa's Brief In Opposition

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QUESTION PRESENTED

Whether Section 801 of the Department of Housing and Urban Development Reform Act of 1989, Pub. L. No. 101-235, 103 Stat. 2057 (1989), is an unconstitutional attempt by Congress to save money by legislatively abrogating express provisions of contracts of the United States to which the United States explicitly pledged its full faith and credit and for which the private party paid independent consideration?

Parties to the Proceeding

Petitioners Jack F. Kemp, *et al.*, omitted from the list of parties to the proceedings in the courts below the following:

Azusa Park Apartments, a California Limited Partnership; Capitola Gardens, a California Limited Partnership; Carondelet Apartments, a California Limited Partnership; Charter Oaks, a California Limited Partnership; Civic Plaza, a California Limited Partnership; Citrus Arms, a California General Partnership; Clayton Gardens, a California Limited Partnership; Columbus Terrace, a California General Partnership; Commerce Senior Citizens, a California Limited Partnership; Covina Manor, a California Limited Partnership; Country Club Village, a California Limited Partnership; El Portal Gardens, a California Limited Partnership; Fairvalley Villa, a California Limited Partnership; Fairway Apartments, a California Limited Partnership; Fallbrook Square Apartments, a California General Partnership; Foothill Gardens, a California Limited Partnership; Foothill Terrace, a California Limited Partnership; Frazier Park, a California Limited Partnership; Grandview Homes, a California Limited Partnership; Hayward Villa, a California Limited Partnership; Kern Villa, a California Limited Partnership; Lake Merritt Apartments, a California General Partnership; Lindley Manor, a California General Partnership; Little Tokyo, a California Limited Partnership; Mayflower Arms, a California Limited Partnership; Merced Gardens, a California Limited Partnership; Millbrook Park Apartments, a California Limited Partnership; Monterey Terrace, a California Limited Partnership; New Hampshire, a California Limited Partnership; Olive Tree Terrace, a California Limited Partnership; Palmdale East Q., a California Limited Partnership; Panorama Park, a California Limited Partnership; Pendleton Arms, a California Limited Partnership; Pleasant Hill Village, a California Limited Partnership; Presidio Park Apartments, a California General Partnership; Primrose Villa, a California General Partnership;

Rosswood Villa, a California Limited Partnership; Runnymede Gardens, a California Limited Partnership; San Gabriel Villa, a California Limited Partnership; San Jose Greens, a California Limited Partnership; Santa Teresa Apartments, a California Limited Partnership; Seaside Villa, a California Limited Partnership; Skypark Apartments, a California General Partnership; Southbay Villa, a California Limited Partnership; Surfside Villas, a California Limited Partnership; Terman Apartments, a California Limited Partnership; Tujunga Gardens, a California Limited Partnership; Tustin Gardens, a California Limited Partnership; Valencia Villa, a California Limited Partnership; Villa Del Comanche, a California Limited Partnership; Villa Olive Oak, a California Limited Partnership; Villa San Dimas, a California Limited Partnership; Villa Topanga II, a California Limited Partnership; Vista Park Chino, a California Limited Partnership; and Wasco Arms, a California Limited Partnership.

TABLE OF CONTENTS

	Page
QUESTION PRESENTED	i
PARTIES TO THE PROCEEDING	ii
TABLE OF CONTENTS	iv
TABLE OF AUTHORITIES	v
INTRODUCTION	1
ARGUMENT	2
I. THE CONTRACT ISSUE	2
A. The Ninth Circuit Correctly Interpreted the Contract	2
B. The Ninth Circuit's Decision Does Not Allow Owners to Reap Windfall Profits	5
II. CONSTITUTIONALITY	9
CONCLUSION	15

TABLE OF AUTHORITIES

Cases **Pages**

Acacia Villa v. Kemp, 774 F. Supp. 1240 (C.D. Cal. 1990), *aff'd*, 955 F.2d 1382 (9th Cir. 1992) 3, 13

Alpine Ridge Group v. Kemp, 955 F.2d 1382 (9th Cir. 1992) 11, 12, 14

Boag v. MacDougall, 454 U.S. 364 (1982) 5

Bowen v. Public Agencies Opposed to Social Security Entrapment, 477 U.S. 41 (1986) . . . 2, 10, 11

El Paso v. Simmons, 379 U.S. 497, *reh'g denied*, 380 U.S. 926 (1965) 9

Federal Housing Administration v. The Darlington, Inc., 358 U.S. 84 (1958), *reh'g denied*, 358 U.S. 937 (1959) 11

Lynch v. United States, 292 U.S. 571 (1934) 2, 10, 12

Perry v. United States, 294 U.S. 330 (1935) 2, 10, 12

Rainier View Associates v. United States Department of Housing and Urban Development, 848 F.2d 988 (9th Cir. 1988), *cert. denied*, 490 U.S. 1066 (1989) 1, 2, 4, 5

Sinking Fund Cases, 99 U.S. 700 (1879) 2

United States Trust Co. v. New Jersey, 431 U.S. 1, *reh'g denied*, 431 U.S. 975 (1977) 9

Statutes and Regulations

Department of Housing and Urban Development Reform Act of 1989, Pub. L. No. 101-235, 103 Stat. 1987 (1989):

§801, 103 Stat. 2057 2

United States Housing Act of 1937, as amended in 1974:

42 U.S.C. §1437c(c) (1976) 10

42 U.S.C. §1437f(c)(1) (1976) 6

42 U.S.C. §1437f(c)(2)(A) (1976) 3

42 U.S.C. §1437f(c)(2)(C) (1976) 3

24 C.F.R. §880.102 (1976) 6

Legislative History

135 Cong. Rec. S16,607 (daily ed. Nov. 21, 1989) (statement of Sen. Sasser) 12-13

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INTRODUCTION

In the absence of any conflict among the federal courts of appeal, the Department of Housing and Urban Development ("HUD") presents this contract dispute in inflated terms to make it appear worthy of this Court's attention. Once HUD's rhetoric is peeled away, the case presents only two issues, neither of which justifies review by this Court.

The issue that occupies two-thirds of the argument in the government's petition is a routine matter of contract interpretation. The government simply asserts that the Ninth Circuit erred in interpreting the contract between HUD and the owners four years ago in *Rainier View Associates v. United States Department of Housing and Urban Development*, 848 F.2d 988 (9th Cir. 1988), and that this Court erred in denying HUD's petition

for a writ of certiorari in that case, 490 U.S. 1066 (1989). Nothing has happened in the meantime to make this issue of contract interpretation any more significant than it was when this Court denied review in 1989.

The case also presents a constitutional issue, but it does not involve, as HUD would have it, a revival of *Lochner* era principles of substantive due process. On the contrary, the issue is merely whether the Constitution permits legislation repudiating HUD's obligation to pay the contract price after performance by a private party under a contract to whose fulfillment the United States has explicitly pledged its full faith and credit.[1] For more than a century, this Court has repeatedly answered that question with a resounding "No." *See, e.g., Sinking Fund Cases, 99 U.S. 700 (1879); Lynch v. United States*, 292 U.S. 571 (1934); *Perry v. United States*, 294 U.S. 330 (1935); *Bowen v. Public Agencies Opposed to Social Security Entrapment*, 477 U.S. 41, 55 (1986). There is no need to grant review in this case to reaffirm that principle again.

ARGUMENT

I. THE CONTRACT ISSUE

A. The Ninth Circuit Correctly Interpreted the Contract.

HUD treats the contract issue raised by this case as if it were an academic exercise in parsing contract language without the benefit of any background facts. Whatever surface plausibility HUD's reading of the contract might have evaporates when the contract is read in its real life context.

The contract dispute in this case involves the mechanism for adjusting for inflation federally subsidized rents under the

[1] The specific provision at issue is Section 801 of the Department of Housing and Urban Development Reform Act of 1989, Pub. L. No. 101-235, 103 Stat. 1987, 2057 (1989) ("Section 801").

Section 8 housing program. The Section 8 housing program was not the government's first foray into the area of subsidized housing. On the contrary, Congress designed the Section 8 program to cure some of the defects of its immediate predecessors, the Section 221(d)(3) and the Section 236 low income housing programs. Under those programs, HUD reviewed developers' requests for rent increases on a case-by-case basis. The procedures HUD used were arbitrary, did not yield a fair rate of return, cost owners large amounts of time and money, and were open to subjective manipulation by HUD employees. *See* Declaration of Jona Goldrich (May 30, 1990) ¶3, Exhibit C1 to Memorandum of Points and Authorities in Support of Plaintiffs' Motion for Partial Summary Judgment, *Acacia Villa v. Kemp*, 774 F. Supp. 1240 (C.D. Cal. 1990), *aff'd*, 955 F.2d 1382 (9th Cir. 1992) ("Goldrich Declaration").

In response to this situation, when Congress created the Section 8 program in 1974, Congress gave the Secretary of HUD the option of entering into contracts under which rent adjustments would be based on "a reasonable formula." Section 8(c)(2)(A) of the United States Housing Act of 1937, as amended in 1974, 42 U.S.C. §1437f(c)(2)(A) (1976). Section 8 also authorized the Secretary to enter into contracts requiring rent adjustments on a case-by-case basis, "to reflect changes in the fair market rentals established in the housing area for similar types and sizes of dwelling units." *Id.* Under Section 8, whether HUD chose contracts calling for adjustments based on a reasonable formula or contracts calling for case-by-case adjustments, the adjustments were not to cause material differences between the rents charged for assisted and comparable unassisted units. Section 8(c)(2)(C) of the United States Housing Act of 1937, as amended in 1974, 42 U.S.C. §1437f(c)(2)(C) (1976).

It is undisputed in the *Acacia Villa* proceeding that because of "negative experiences with the delays and extraordinary

administrative inconveniences associated with case-by-case adjustments, [the plaintiffs] participated in the Section 8 program only because the Section 8 HAP contracts, unlike the Section 221(d)(3) and Section 236 program contracts, provided for rent adjustments to be computed at least annually according to an equitable, timely and simplified formula to be published in the *Federal Register*." Goldrich Declaration ¶3.

HUD was fully aware that the attitudes of the *Acacia Villa* owners were shared by many other potential developers of Section 8 housing. The majority of potential Section 8 developers were unwilling to take part in the new program if it involved the inconvenience, delays, and inequitable results produced by HUD's case-by-case adjustments of Section 221(d)(3) and Section 236 rents. For this reason, in the Section 8 program, HUD did not use contracts that called for case-by-case adjustments. HUD opted to offer all developers contracts that explicitly called for rent to be adjusted "by applying the applicable Automatic Annual Adjustment Factor most recently published by the Government." HAP Contract §1.8(b)(2). As the Ninth Circuit held:

> Under the statute, HUD could choose either a market survey method (described in the first clause of Section 8(c)(2)(A)) *or* a formula method (described in the second clause of Section 8(c)(2)(A)). In the contract, HUD elected the formula method.

Rainier View Associates, 848 F.2d at 991.

These background facts, which HUD completely ignores, demonstrate the implausibility of HUD's contention that the parties intended to "permit HUD to abandon entirely the formula method it chose and to adjust rents solely on the basis of a market survey." *Id.* They highlight the correctness of the Ninth Circuit's interpretation of the contracts here at issue as requiring rents to be adjusted by multiplying the previous year's rent by a published inflation factor. As a result of this background, this

Court denied review of the contract issue when HUD requested it in 1989, 490 U.S. 1066 (1989), and should do so again today. "[T]his Court is not a forum for the correction of errors," *Boag v. MacDougall*, 454 U.S. 364, 368 (1982) (Rehnquist, J., dissenting), and should not grant review merely to correct a purported error in contract interpretation that raises no issues of broader applicability.

B. The Ninth Circuit's Decision Does Not Allow Owners to Reap Windfall Profits.

Throughout its petition, HUD attempts to induce the Court to grant review by portraying the owners as rapacious landlords who have gulled the Ninth Circuit into permitting them to reap enormous windfall profits by charging "excessive rents" beyond those permitted by the statute and the contracts. *See, e.g.*, Petition at 14. HUD stresses that the statute and the contracts place a ceiling on rents, as if the owners had persuaded the Ninth Circuit to ignore those obvious provisions. In fact, neither the owners nor the Ninth Circuit have ever denied that "[t]he statute requires the Secretary to ensure comparability." *Id.* Neither the owners nor the Ninth Circuit have contended that the statute or the contracts permit the published "Adjustment Factors [to] be mechanically applied when to do so would yield excessive rents." *Id.* The owners and the Ninth Circuit fully recognize the Secretary's statutory and contractual authority and obligation to see to it that rents paid under the program increase at the same rate as rents for unassisted units. *See Rainier View*, 848 F.2d at 989. The owners contend and the Ninth Circuit held only that the contracts which HUD drafted and signed were designed to achieve and maintain comparability in rent adjustments through a formula which HUD would modify as appropriate, but which it could not abandon because it did not like the results. *See id.* at 991.

HUD asserts that only case-by-case comparability studies can take into account all the myriad small details that affect the

rental value of an apartment. Therefore, HUD claims that if it adjusts rents simply by applying published inflation factors, it will not be able to avoid violating the limitations on rent adjustments imposed by the statute and the contract. According to HUD, rent adjustment must be based on case-by-case comparisons to prevent the annual rent adjustment process from causing material differences between rents for assisted and unassisted units. HUD's argument is unfounded and rests on a confusion between what must be done to *establish initial rents* and what must be done to *adjust those rents for inflation.*

HUD negotiated the initial rent for each apartment with the owners. As a result of HUD requirements, Section 8 apartments were often located in neighborhoods where land values were high. HUD frequently mandated costly features rarely found in moderate-income apartments. Furthermore, HUD required developers to pay Davis-Bacon Act wages and to incur additional operating and administrative costs to comply with various HUD regulations. Congress recognized that because of the special features of Section 8 apartments and the special costs associated with building and operating them, initial rents for Section 8 apartments would often need to be up to 20 percent higher than the levels established as "fair market rentals" by the Secretary of HUD. *See* Section 8(c)(1) of the United States Housing Act of 1937, as amended in 1974, 42 U.S.C. 1437f(c)(1) (1976). The statute does not define the term "fair market rentals." The original HUD regulations interpreting this term defined it as "the rent, including utilities (except telephone), ranges and refrigerators, parking, and all maintenance, management and other services, which, as determined at least annually by HUD, would be required to be paid in order to obtain privately developed and owned, newly constructed rental housing of modest (non-luxury) nature with suitable amenities and sound architectural design meeting the objectives of the HUD Minimum Property Standards." 24 C.F.R. §880.102 (1976).

When HUD negotiated initial rents, it took into account all the individual features of each apartment, including the many special features required by HUD. The initial rent represented HUD's estimate of the appropriate rent for each apartment in light of all the facts and the constraints imposed by the statute and HUD's own regulations. Detailed comparisons with other apartments may have been appropriate as part of that process, even though the most comparable apartments in the unassisted market were often quite different from Section 8 apartments.

Such comparisons are neither necessary nor appropriate parts of the process of *adjusting rents* for inflation. The annual rent adjustments called for by the statute and by the contracts focus only on the appropriate *percentage change* in the initial rent. They are intended to account for the *rate* of inflation or deflation of rents in whatever market area HUD deems appropriate. They do not allow HUD, in the guise of insuring comparability, to repudiate unilaterally the initial rents HUD negotiated with the developers, and on which the developers relied when the contracts were entered into and the apartments built.

Neither logic nor experience suggests that the kinds of differences between apartments that can be accounted for only on a case-by-case basis affect the *inflation rate* for apartment rents. Once the initial rent is determined, taking into account all relevant features of the assisted apartment and the rents of unassisted units, application of a factor that accurately represents inflation or deflation in the appropriate rental market for apartments in the same price range, of the same general type, and with the same number of bedrooms, will produce an appropriate adjustment.

HUD can and should perform checks to insure that the inflation rates it publishes produce accurate results, and should modify the factors if they do not. If, for example, the market in which an apartment is located has experienced a lower or higher

rate of inflation than the larger market of which it forms part, HUD can and should publish adjusted inflation factors that reflect conditions in that sub-market and that will apply to all Section 8 units in the sub-market. None of this, however, justifies abandoning use of the published factor and a return to arbitrary case-by-case adjustments by untrained HUD clerks under pressure from their superiors to reduce HUD's obligations.

HUD assumes throughout its Petition that its comparability studies constitute an accurate benchmark against which to measure rentals. Nothing in the record supports this contention. On the contrary, the district court in *Rainier View* held that HUD performed its comparability studies so deficiently that they violated procedural due process. *Rainier View Associates v. United States*, No. C83-997R (W.D. Wash. Feb. 28, 1984), Order re Cross Motions For Summary Judgment, reproduced in Petition for a Writ of Certiorari to the United States Court of Appeals for the Ninth Circuit, *United States v. Rainier View Associates*, No. 88-1515, at 30a. Appraisals carried out by HUD clerks without any "guidelines to ensure that the comparability reviews are conducted pursuant to some consistent system or methodology," *id.*, are much less accurate guides to fair rentals than the rents determined by multiplying initial rents by the inflation factors HUD's Central Statistical Offices produce.

It is undisputed in *Acacia Villa* that "[c]ontinued failure to receive the full amount of the rent adjustments required by the HAP contracts may put some of the projects in precarious financial conditions. Inadequate cashflow will make it difficult or impossible to maintain the buildings properly and to take all of the security measures which are becoming increasingly necessary at certain complexes." Goldrich Declaration ¶23. The uncontroverted evidence, therefore, shows inadequate rents rather than windfalls.

The owners do not ask for rent adjustments larger than the statute and the contracts permit. What the owners do ask is that HUD honor its contracts and not attempt to use arbitrary case-by-case adjustments to reduce rents below the levels called for by the contracts. It is not a windfall to receive a rent set by applying inflation factors published by HUD to the initial rent negotiated by HUD and determined by HUD to fall within the range permitted by the statute and by HUD's regulations. The contracts explicitly call for precisely that mechanism of rent adjustment, and the owners would not have entered the program if the contracts had called for case-by-case adjustments. As a matter of law, "gains reasonably to be expected from [a] contract" are not windfalls. *United States Trust Co. v. New Jersey*, 431 U.S. 1, 31, *reh'g denied*, 431 U.S. 975 (1977). *Accord, El Paso v. Simmons*, 379 U.S. 497, 515, *reh'g denied*, 380 U.S. 926 (1965). There is, therefore, no need for this Court to grant review to avoid a purported windfall at the government's expense.

II. CONSTITUTIONALITY

The Ninth Circuit held that the Constitution does not permit Congress to save money by repudiating its explicit contractual commitments after accepting goods and services under a contract with a private party to which the United States has pledged its full faith and credit. The logic of the Ninth Circuit's holding is simple and non-controversial. The decision rests on well-established principles of constitutional law that do not require review by this Court. The Ninth Circuit reached its conclusion on the following basis:

1. The owners' contract right to rents determined by applying the published Automatic Annual Adjustment Factor is a vested right.
2. Section 801 substantially impairs those rights.

3. The congressional purpose in passing Section 801 is not sufficiently important to permit abrogation of those rights.

This Court has repeatedly taught that contract rights supported by independent consideration are vested. *See Lynch*, 292 U.S. 571; *Perry*, 294 U.S. 330; *Bowen v. Public Agencies*, 477 U.S. at 55. The vested nature of the rights here at issue is highlighted by the fact that in the statute and in the contracts the United States explicitly pledged its full faith and credit. *See* 42 U.S.C. §1437c(c) (1976); Contract between HUD and Antelope Valley Apartments §1.3(a). (Exhibit 2C to Goldrich Declaration).

The principle that the government must honor contracts for goods and services with private parties is fully compatible with this Court's decision in *Bowen v. Public Agencies*. Indeed in that case, this Court explicitly recognized that "the Federal Government, as sovereign, has the power to enter contracts that confer vested rights, and the concomitant duty to honor those rights." 477 U.S. at 52 (citations omitted). This Court explicitly distinguished the rights at issue in *Bowen v. Public Agencies* from those which had been held to constitute "property" within the meaning of the Fifth Amendment. It pointed out that the provision at issue in *Bowen v. Public Agencies* "constituted neither a debt of the United States, see *Perry v. United States*, *supra*, nor an obligation of the United States to provide benefits under a contract for which the obligee paid a monetary premium, see *Lynch v. United States*, *supra*." 477 U.S. at 55.

HUD asserts that this case does not "repudiate a legislatively promised benefit for which private parties paid consideration as in *Lynch*," Petition at 21, but the facts belie HUD's contention. The owners entered into contracts that stipulated an initial rent which would be adjusted *only* under a formula set forth in the contract. In consideration for HUD's promise to pay rent on that basis, the owners expended hundreds of millions of

dollars on the construction of apartment buildings, made the apartments available to low-income tenants, and operated the apartments in accordance with HUD's rules and regulations under the Section 8 housing program. This is exactly the sort of bargained for right which this Court distinguished from the situation it confronted in *Bowen v. Public Agencies*. *See* 477 U.S. at 55.

Contrary to HUD's contentions, the Ninth Circuit fully recognized the power of Congress to pass "curative" legislation to undo a judicial interpretation of a preexisting statute, even when the curative legislation extinguishes claims against the government. *Alpine Ridge Group v. Kemp*, 955 F.2d 1382, 1386 (9th Cir. 1992), Petition at 10a. The Ninth Circuit acknowledged that Congress has authority to amend the laws and thereby to extinguish claims to *benefits gratuitously conferred* by statute, even after a court has interpreted the statute as creating certain rights. The Ninth Circuit correctly held, however, that this power does not extend to extinguishing *bargained for contract rights* supported by independent consideration. *Id.* As the Ninth Circuit stated, the case the government relies upon, *Federal Housing Administration v. The Darlington, Inc.*, 358 U.S. 84 (1958), *reh'g denied*, 358 U.S. 937 (1959), involved a refusal to interpret contracts as containing *implied* provisions foreclosing the exercise of sovereign power by the government. *The Darlington* does not suggest that an *explicit* contractual right, for which independent consideration has been provided and to which the full faith and credit of the United States has been pledged, is not vested because Congress may abrogate it at any time, for any reason, or no reason. The Ninth Circuit's conclusion that the owners' rights are vested and constitute property reflects the settled jurisprudence of this Court.

In the Ninth Circuit, HUD did not contest that Section 801 substantially impairs the owner's exercise of their vested contract rights. *Alpine Ridge Group*, 955 F.2d at 1387, Petition at

12a. In this Court, HUD argues, albeit only in a footnote, that there is no substantial impairment because rent increases determined by using a properly adjusted inflation factor "*could* presumably have produced the same financial result for Section 8 landlords as the approach HUD adopted...." Petition at 20 (emphasis added). Even if in a given case application of an adjusted inflation factor did by chance lead to the same results as the HUD comparability study, the owners would still be damaged by having to submit to a cumbersome, arbitrary, time-consuming, and expensive process not provided for in their contract. HUD makes no effort to refute the owners' evidence that after their experience with previous programs, they would not have entered the Section 8 program had they known that HUD would attempt to make case-by-case rent adjustments in the Section 8 program. Furthermore, that a properly adjusted inflation factor *could* lead to the same dollar result as a comparability study in a given case, is no evidence that the owners have not suffered serious financial harm through HUD's use of comparability studies to reduce its rent obligations.

Having held that Section 801 substantially impairs vested contract rights that constitute property, the Ninth Circuit inquired whether the congressional purpose was sufficiently important to justify such impairment. Neither in the court below nor in this Court does HUD contend that the government may abrogate vested contractual rights of parties to a contract with the government solely to save money. *See Alpine Ridge Group*, 955 F.2d at 1387, Petition at 13a; Petition at 21; *cf. Lynch*, 292 U.S. 571; *Perry*, 294 U.S. 330. Section 801 is on its face a provision designed to reverse the Ninth Circuit's *Rainier View* interpretation of HUD's obligations under the HAP contracts and thereby to save the costs involved in complying with the contracts. In the words of one of the bill's principal sponsors, Section 801 was a "fix" intended to "save the Government hundreds of millions, if not more than a billion dollars." 135

Cong. Rec. S16,607 (daily ed. Nov. 21, 1989) (statement of Sen. Sasser).

Both in the courts below and in this Court, HUD attempts to save Section 801 from invalidity by inventing other purposes for the legislation. In this Court, HUD points to three purported goals of Section 801 beyond saving money: 1) to put an end to litigation with its resulting uncertainty; 2) to avoid excessive rents; and 3) to correct flaws in HUD's application of comparability studies in the past. Petition at 22. The courts below fully considered and properly rejected each of these purported justifications for the statute.

As the district court stated in *Acacia Villa*, 774 F. Supp. at 1250, Petition at 59a, the first justification, the resolution of the dispute, "is little more than bootstrapping. The dispute is about the fact that the contracts have been interpreted adversely to the government by the Ninth Circuit; the government now wants to avoid paying the project owners the amount that the contracts, as so interpreted, require. Again, the government is only concerned with dollars."

The government's purported desire to "reinstate the program's market-rent premise," Petition at 22, is a thinly veiled euphemism for paying less than the contracts require. The purpose is simply to save money.

The purported objective of correcting flaws in HUD's past use of comparability studies is no justification at all. Since application of comparability studies is a violation of the owners' contract rights, the government cannot justify application of the studies on the ground that it seeks to apply them more equitably where the government had no right to apply them at all. *Acacia Villa*, 744 F. Supp. at 1250, Petition at 58a-59a.

Because none of HUD's purported objectives for passage of Section 801 resist critical analysis, the Ninth Circuit concluded that Congress enacted Section 801 solely to save money,

as is evident from the face of the statute and from its legislative history. *Alpine Ridge Group*, 955 F.2d at 1387-88, Petition at 14a.

The Ninth Circuit's decision that Congress could not abrogate HUD's contractual obligations and the United States' pledge of its full faith and credit simply to save money rests on well established principles and does not require review by this Court.[2]

[2] Because the Ninth Circuit concluded that the legislation had been passed solely to save money and therefore violated due process, it did not reach the question of whether Section 801 would violate the due process clause even if it had some purpose other than simply saving money. The owners contend that even in that case Section 801 would violate due process. The Ninth Circuit similarly did not reach the owners' contention that Section 801 violates not only the due process clause, but also the taking clause of the Fifth Amendment and the prohibition in the Fourteenth Amendment against questioning the public debt. These remain viable alternative grounds for holding the statute unconstitutional.

CONCLUSION

This case presents only a routine issue of contract interpretation and a constitutional question that is fully resolved by application of the undisputed principle that the United States may not, in order to save money, refuse to honor its contractual obligations to a private party that has fully performed its side of the bargain when the United States has pledged its full faith and credit to the fulfillment of those obligations. The case poses no questions that require review by this Court.

Respectfully submitted,

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